of the alternative minimum tax (AMT). AMT was designed to reduce the ability of higher income individuals to escape taxes by using certain deductions. It applies a parallel tax system on a broader base of income, and taxpayers pay the greater amount of their regular tax or the AMT. The AMT already was expected to rise significantly prior to the law's passage, primarily because its exemption is not indexed for inflation.

Income tax rate reductions accelerate the growth in the total amount paid under AMT since AMT rates remain unchanged, although the new law temporarily increases the amount of income not subject to AMT through 2004. Currently only 2 percent of farmers pay AMT, but that number is expected to rise to 33 percent by 2010 without further AMT relief. If AMT were held at 2001 levels, the 10-year sum of the income tax cut for farmers would be $26 billion. Therefore, the rising incidence of AMT reduces farmers' income tax cut by more than one-fourth over the decade to $19 billion.

The law also makes changes that will greatly reduce the number of farm estates affected by the Federal estate tax. Before repeal of the estate tax in 2010, the most significant change is to increase the dollar amount of property exempted from tax from the current $675,000 to $3.5 million by raising the unified credit. The unified credit allows each estate to transfer a certain lifetime amount of property free of estate and gift taxes. The new law also gradually reduces the maximum estate tax rates from 55 to 45 percent and expands the availability of deductions for donating conservation easements. The law repeals the family business deduction when exemption from the unified credit reaches $1.5 million, exceeding the $1.3 million currently allowed under the family business deduction and unified credit.

While these changes will reduce the amount of Federal estate taxes owed, the most dramatic effect will be a sharp drop in the number of farm estates required to file an estate tax return. By 2004, when the amount exempted by the unified credit reaches $1.5 million, only about a third of those farm estates that currently are required to file would need to file an estate tax return. This represents large cost savings for farm estates that are no longer required to file. However, because of the extended phase-in, larger estates may still face considerable complexity, since they may still owe tax and be required to file, depending on date of death of the property owner.

The number of estates owing taxes and the amount of estate taxes owed will decline more gradually, with both falling about 10 percent in 2002. Over the next decade, farmers are expected to save about $3 billion in Federal estate taxes.

The new law reduces both income and estate taxes for most taxpayers, including most farmers. While savings begin in 2001, many reductions are implemented gradually. Without future action, however, the law expires in 2011, and provisions revert to pre-reform levels. AO

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Livestock, Dairy, & Poultry

Financial Prospects for Hog Producers Generally Favorable

The national hog inventory this year has remained at 59.1 million head, about the same as last year, despite relatively favorable returns. Over the last 18 months, hog prices have averaged in the mid-$40s per cwt, topping producers' mid-$30s breakeven (cash) costs. Producers have signaled intentions to increase the number of sows farrowing over the next 6 months, according to the USDA's June *Hogs and Pigs* report. Producers plan to have 1 percent more sows farrow in June-August and 2 percent more in September-November than actual farrowings in these periods a year earlier.

The changing structure of hog production and the industry's financial problems in late 1998 and most of 1999 have muted hog producers' response to prospects of favorable returns. Many smaller producers exited the industry in the late 1990s. Smaller producers that remain may still be recovering from financial problems. Lenders are also likely to be more cautious about financing hog operations.

If producers follow through with their farrowing intentions, and if only a small increase in pigs per litter occurs as expected, the June-August pig crop should be up about 1 percent from a year ago and the September-November number up 2 percent. These projections imply a January-March 2002 hog slaughter of nearly 25 million head and second-quarter slaughter of nearly 24 million head. With dressed weights increasing slightly, first-half 2002 pork production is expected to be 2-3 percent higher than a year earlier.

With expectations of continued positive returns for hog producers in the coming months, the December 2001-May 2002 pig crop should increase nearly 3 percent over a year earlier. Feed costs are expected to remain unchanged into 2002 as a large corn crop and record soybean crop move to market. Although hog prices are expected to moderate in the coming months, producers' returns should remain positive. The larger expected pig crop and slightly heavier dressed weights should boost pork production in the second half of 2002 by 3-4 percent.

Hog prices climbed into the mid-$50s per cwt in late spring and early summer as slaughter rates declined seasonally. Also contributing to the rise were strong exports, brisk demand for bacon, especially in the fastfood industry, record retail beef prices (which make pork more attractive to consumers), and a slight decline in broiler supplies. As slaughter increases seasonally in late summer, prices are expected to moderate. In the late fall, when slaughter reaches a seasonal peak, hog prices are expected to drop into the

Briefs

Structural Changes in the Hog Industry

The structure of hog production has changed dramatically in recent years, affecting the national average of pigs per litter as well as the production cycle (contraction and expansion). Large producers—those with inventories of 5,000 head and over—now account for nearly 75 percent of the nation's hogs, compared with 27 percent in 1994.

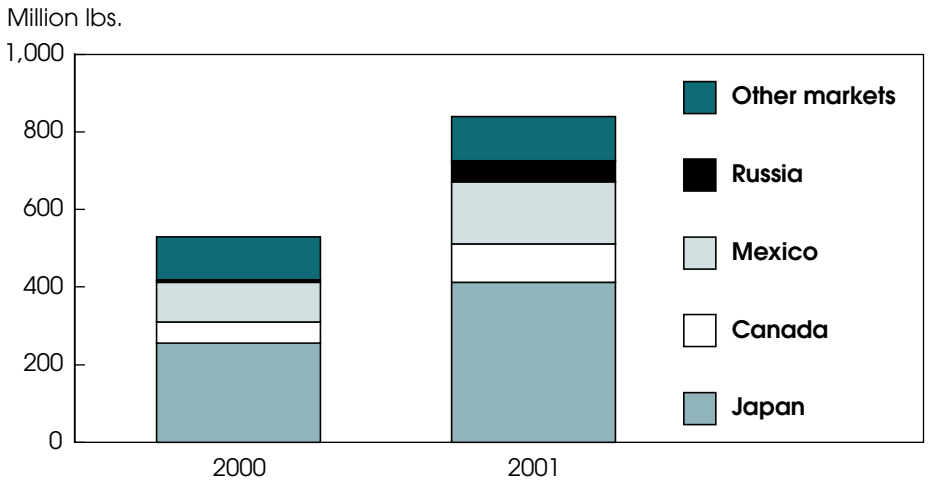
As the proportion of the industry consisting of larger producers has increased, gains from economies of size have largely been realized, and the overall rate of increase in pigs per litter has slowed. During 1996-97, pigs per litter rose over 2 percent per year but has since moderated to less than 1 percent per year. Future increases in pigs per litter could slow even more because the hog production industry is already dominated by large operations.

Pigs per litter in larger operations was 8.96 in 2000, compared with 8.74 in 1994, less than a 3 percent increase. The rate for operations with less than 5,000 head increased from 8 pigs in 1994 to 8.48 pigs in 2000, a 6 percent increase. The greater increase for smaller operations was likely because less efficient operations were going out of business and a larger proportion of the pig crop was coming from operations with 1,000 to 5,000 head. The U.S. average for pigs per litter is now only 0.13 less than for larger producers, compared with 0.55 in 1994.

Production expansion for larger and mid-sized producers is more complicated than in the recent past. The expansion process now includes securing financing, obtaining building and waste management permits from state and local authorities, and hiring and training staff. Also, vertical coordination through either marketing or production contracts is now prevalent, rather than spot-market sales. These factors likely mute the peaks and valleys of the hog cycle.

In contrast, many producers 15 to 20 years ago maintained multi-use buildings for rapid repopulation of a hog herd when returns turned favorable. Necessary construction was accomplished without administrative procedures for securing waste permits. Thus, producer responses to positive or negative returns tended to be more rapid and often sharper in the aggregate.

U.S. Pork Exports Up Sharply in First-Half 2001



January-June data. Carcass-weight equivalent.

Economic Research Service, USDA

low-$40s. Prices are expected to average $46-$47 per cwt in 2001, compared with $44.70 in 2000.

With only modest changes in pork production and trade in 2002, hog prices are expected to average in the mid-$40s next year. However, some uncertainty exists about how the imposition of Japan's import safeguard will affect U.S. exports to that market. (The safeguard is a World Trade Organization-sanctioned mechanism for protecting Japanese pork producers from import surges.) Exports to other markets are expected to remain strong.

Retail demand continues to be strong as composite retail pork prices averaged 4 percent higher in second quarter 2001 than a year ago. Average retail pork prices are expected to rise 3-4 percent in calendar 2001 and to be unchanged in calendar 2002.

U.S. pork exports are forecast at a record 1.54 billion pounds this year and slightly less in 2002 (1.42 billion pounds). U.S. pork exports in the first half of 2001 ran 33 percent ahead of last year, due primarily to very large shipments of fresh and frozen pork cuts to Japan. For a variety of reasons—high U.S. beef prices, foot-and-mouth disease outbreaks in Europe, lower domestic hog slaughter—Japanese importers contracted for such large quantities of pork from the U.S., Denmark, and Canada that the safeguard threshold of 183,850 metric tons (product-weight equivalent) was exceeded in June. On August 1, the Japanese Government imposed the safeguard, which increased the minimum price of all pork cuts imported into Japan by 24.6 percent. The safeguard will remain in place until March 31, 2002, the end of the Japanese fiscal year.

The last time the safeguard was in place—July 1996 through June 1997—Japanese imports slowed dramatically, particularly frozen pork cuts. This time, however, its effect on Japan's pork imports is uncertain.

U.S. pork imports are forecast at 916 million pounds in 2001 and 960 million in 2002, compared with 967 in 2000. Imports in the first 6 months of 2001 dropped 12 percent from a year ago

because Canada and Denmark appear to have diverted pork products to Japan that were originally destined for the U.S. The extent to which Japanese pork imports slow as a result of the safeguard will strongly influence the amount these countries ship to the U.S. in the second half of 2001.

Live hog imports into the U.S. are forecast at 5.3 million head for both 2001 and 2002, compared with 4.36 million head in 2000. The rapid evolution of both a feeder-pig export sector in Canada and a hog-finishing sector in the Corn Belt states that was traditionally run as farrow-to-finish operations, is stimulating imports.

Continued expectations for low feed prices are also contributing to higher imports. Live hog imports from Canada during the first half of 2001 were almost 2.5 million head. AO

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Livestock, Dairy, & Poultry

Mandatory Price Reporting for Livestock Industry

Livestock packers and importers whose operations exceed certain levels must now report detailed information to USDA on price, quantity, and characteristics of livestock they buy and sell. April 2, 2001 marked the first day of implementation of USDA's Mandatory Price Reporting (MPR) system, mandated by the Livestock Mandatory Price Reporting Act of 1999.

The law was a government response to demand by livestock producers for more information on meat industry prices. The purpose of MPR is twofold: to provide all livestock producers with timely market information to enable them to operate successfully in a recently changed economic environment, while also meeting consumer demand for meat and meat products.

MPR applies to packer purchases of cattle, hogs, and sheep, as well as to prices of boxed beef, boxed lamb, and carcass lamb. USDA requires federally inspected processing facilities to comply with the MPR reporting schedule if average annual slaughter over the preceding 5 years reached 125,000 head for cattle, 100,000 head for hogs, or 75,000 head for lambs. The MPR system requires cattle packers to report specific price and quantity information twice daily. Hog packers must report three times per day; lamb processors report once daily. All livestock packers supply a weekly summary.

USDA had been reporting market price information through its Market News system, but MPR differs in several important ways. Participation in the Market News system was voluntary; MPR is not. MPR also requires reporting of price and quantity information in much greater detail. Under MPR, packers must report the terms of sales made through markets other than traditional public markets. In keeping with recent structural changes in the U.S. meat/livestock industry, MPR focuses on negotiated private purchases and formula and contract sales. Packers must report specific terms of formula and contract purchases, thereby revealing information previously treated as proprietary.

Livestock marketing has evolved from pricing on the basis of live animals to a basis of quality incentives assigned to the characteristics of carcasses, as well as to specific carcass measurements. MPR takes account of this evolution, and requires packers to report full schedules of quality premiums and discounts paid for carcasses according to their quality characteristics, such as age, fat content, and marbling.

The meat/livestock industry itself has evolved over the past 20 years and is characterized by fewer, larger packers and fewer, larger producers. Vertically coordinated/integrated production by contractual arrangements enables steady supplies of uniform animals. This, in turn, facilitates the supply of meat products bearing specific characteristics desired by consumers.

Many small independent livestock producers, who continue to market small numbers of animals through spot markets, point to the restructured industry as a justification for MPR. In fact, the Mandatory Price Reporting Act of 1999 was conceived when small producers successfully argued that proprietary price information contained in production and marketing contracts was not publicly available and therefore did not fully provide transparency in the market place.

After several startup delays, USDA implemented a schedule of 56 daily and 35 weekly livestock and meat reports covering national and regional prices and quantities. Six weeks after startup, an understating of cutout values for beef carcasses and primals (the major components of carcasses) became apparent. The cause of the under-pricing was identified as a software programming error, and has been rectified.

Frequent interruptions have also occurred in the MPR reporting schedule, reflecting the difficulty of protecting respondent confidentiality in an industry dominated by a few large firms. The Livestock Mandatory Reporting Act requires that information obtained by the MPR program be released to the public only if the identity of a respondent is not disclosed and the information conforms to aggregation guidelines established by the Secretary of Agriculture. In implementing the new law, USDA first adopted a set of standards used widely by government data collection agencies to ensure respondent confidentiality. The guideline, often termed the "3/60 Rule," states:

"Submitted information will only be published by USDA if: (1) It is obtained from no fewer than 3 packers… representing a minimum of three companies; (2) the information from any one packer… represents not more than 60 percent of the information to be published…."

Because the structure of the U.S livestock/meat industry has evolved toward fewer, larger packing firms, and data are